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CHARLES ELMORE CROPLEY
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Supreme Court of the United States

OCTOBER TERM, 1941.

No. 781.

ROYAL INDEMNITY COMPANY, - - - Petitioner,

versus

UNITED STATES OF AMERICA, - - - Respondent.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Sixth Circuit and Brief in Support Thereof.

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Supreme Court of the United States

OCTOBER TERM, 1941.

No._____

ROYAL INDEMNITY COMPANY, - - *Petitioner,*

v.

UNITED STATES OF AMERICA, - - *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

To the Honorable, the Supreme Court of the United States:

Your petitioner respectfully shows:

I.

SUMMARY STATEMENT OF THE MATTER INVOLVED.

In the year 1918 Louisville Woolen Mills and three other corporations were wholly owned by American Textile Woolen Company. The five corporations were therefore affiliated within the meaning of Section 240 of the Revenue Act of 1918, which mandatorily required that affiliated corporations should make a con-

solidated return instead of individual returns, and that the tax should be computed upon such consolidated return and assessed upon the respective affiliated corporations in such proportions as may have been agreed upon among them, or in the absence of any such agreement, on the basis of the net income properly assignable to each.

Notwithstanding the mandatory provisions of Section 240, the Louisville Woolen Mills and its affiliates did not file a consolidated return for the tax year 1918, but each filed an individual return. In due course there was assessed against each of the affiliates the tax shown to be due on their respective individual returns. Within the time provided by law the Louisville Woolen Mills paid three quarterly installments of the tax assessed against it on its individual return, but shortly before December 15, 1919, the date on which the last installment, amounting to $32,341.24, became due, it filed with the Commissioner of Internal Revenue a request that the balance of the assessment be abated by giving it the benefit of a special assessment as authorized by Sections 327 and 328 of the Revenue Act of 1918 (which in substance authorized the Commissioner, if he found that owing to abnormal conditions affecting the capital or income of a corporation assessment of the tax under the general provisions of the Act would work upon such corporation an exceptional hardship, to assess the tax against such corporation so that the tax would bear the same ratio to the net income of the taxpayer as the average tax of representative corporations engaged in like or similar trade

or business bore to their average net income). At the time the claim for abatement was filed Louisville Woolen Mills asked that payment of the fourth installment be postponed until its claim for abatement had been acted upon by the Commissioner, which request was granted, the taxpayer being required, however, to execute the following bond:

"Know All Men By These Presents:

That the Louisville Woolen Mills, a Kentucky corporation, doing business in Louisville, Kentucky, where their offices are, has this day filed Form 47, asking an abatement of their tax in the sum of $32,341.24.

"Now, Therefore, in consideration of withholding collection and of said taxes at this time and until such time as the Honorable Commissioner of Internal Revenue may pass upon the claim for abatement of said assessed taxes filed by the principal herein, and in order to protect the United States Government and Elwood Hamilton, Collector of Internal Revenue of the Kentucky District, against any loss, cost or damage by reason of the said claim for abatement, the Louisville Woolen Mills, of Louisville, Kentucky, principal, and the Royal Indemnity Company, of New York, surety, hereby bind themselves, jointly and severally, and their several heirs, executors, administrators, successors and assigns to pay to the said Elwood Hamilton, Collector of Internal Revenue in and for the Collection District of Kentucky, the sum of $32,341.24, or as much thereof, if any, as the said Louisville Woolen Mills may be required

by the United States of America to pay on account of said assessment, together with interest thereon at the rate of one per cent per month from the 15th day of December, 1919, and together with all costs and penalties thereon; and the said principal and surety do further bind themselves, jointly and severally, their several heirs, executors, administrators, successors and assigns, to hold the said Elwood Hamilton, Collector of Internal Revenue as aforesaid, entirely harmless from all loss, costs, and damages he may sustain by reason of his having given to the said principal, that is, the Louisville Woolen Mills, an extension of time within which to obtain a final ruling from the Honorable Commissioner of Internal Revenue as to the liability of the said Louisville Woolen Mills for the said assessment; and, further, to pay the sum of $32,341.24, or as much thereof, if any, as the Honorable Commissioner of Internal Revenue shall find from his rulings to be due to the United States of America from the said Louisville Woolen Mills on account of the said assessment, with interest thereon at the rate of one per cent per month from the 15th day of December, 1919, together with all costs and penalties thereon which may accrue.

"In Testimony Whereof, witness the signature of the Louisville Woolen Mills, as principal, and the Royal Indemnity Company, of New York, as surety, this 15th day of December, 1919.

Louisville Woolen Mills,
Per R. H. Wintersmith, Agent.

Royal Indemnity Company,
By Henry C. Bedinger,
Atty. in fact."

At the time this bond was executed no consolidated return had been filed by the Louisville Woolen Mills or any of its affiliates.

Nearly one year after the execution of the bond, and without having theretofore disposed of the claim for abatement, the Commissioner ruled that the Louisville Woolen Mills and the other corporations hereinbefore referred to were affiliated within the meaning of Section 240 of the Revenue Act of 1918, and that a consolidated return instead of individual returns should be filed for that year. In accordance with such ruling the parent company, American Textile Woolen Company, filed such consolidated return. Thereafter the Commissioner ruled that an agreement existed between the corporations to the effect that all of the tax shown to be due on the consolidated return should be assessed against the parent corporation alone, and he accordingly proposed such an assessment.

At this stage of the proceeding, and in reliance upon the Commissioner's ruling that a consolidated return was required and that the tax assessed in respect thereof should all be paid by the parent company, Louisville Woolen Mills contributed to the parent company $30,000 toward the consolidated tax liability, which amount, together with other funds, was turned over by the parent company to the Collector as a payment on account of the ultimate consolidated liability.

The parent company then appealed to the Board of Tax Appeals from the Commissioner's decision and ruling to the effect that an agreement existed between

the parent company and its affiliates under which all the tax resulting from the consolidated return should be assessed against the parent company. While Louisville Woolen Mills and the other three subsidiaries of the parent company were originally permitted to appear in the Board of Tax Appeals case, subsequently at the hearing an order was made eliminating them on the ground that they were not proper parties to the appeal. The Board of Tax Appeals upheld the Commissioner in his contention that there was an agreement between the corporations that all the tax shown to be due by the consolidated return should be assessed against the parent company alone. The opinion of the Board was rendered June 12, 1931, and final order under Rule 50 of that Board was entered on January 16, 1932 (23 B. T. A. 670). The parent company appealed to the Circuit Court of Appeals for the Sixth Circuit, which affirmed the Board (68 Fed. (2d) 820). This Court denied certiorari (293 U. S. 558).

During the entire period of twelve years and one month which intervened between the filing of the claim for abatement and execution of the bond, and the entry of the order of the Board of Tax Appeals, the Commissioner made no ruling that Louisville Woolen Mills was liable for any amount of tax on account of the assessment made on its individual 1918 return. However, on August 23, 1932, which was twelve years and eight months after the execution of the bond, and more than one year and two months after the Board of Tax Appeals had decided that all of the taxes of the affiliated corporations for the year 1918 were assess-

able against and collectible from the parent corporation, American Textile Woolen Company, alone, the Commissioner undertook to fix liability on the bond in the following letter addressed to Louisville Woolen Mills:

> "Your claim is for abatement of part of the tax reported on your separate 1918 return and is a claim for special assessment under Sections 327 and 328 of the Revenue Act of 1918. During the year 1918 your company was a subsidiary of American Textile Woolen Company, and computation of the profits tax of the consolidation under Sections 327 and 328 of the Revenue Act of 1918 was allowed by the Bureau. The Bureau's computation of the consolidated tax was appealed to the United States Board of Tax Appeals by your parent company on an issue relative to the allocation of the tax, and the Board's order entered January 16, 1932, in effect allocates to your company the amount of tax previously assessed on your return. Your claim for the abatement of part of such assessment will therefore be rejected."

At the time said letter was written Louisville Woolen Mills was hopelessly insolvent and paid no part of the sum mentioned in the bond, and thereupon demand was made upon the surety, Royal Indemnity Company, petitioner herein, for payment, and payment was refused upon the ground that there had been no breach of the bond. Suit was then brought in the United States District Court for the Western District of Kentucky to recover on the bond. The case was

tried upon the pleadings, which set out the facts as hereinabove stated. The District Court gave judgment against the surety, petitioner herein, for the full amount of the bond plus interest, but denied it the benefit of the contribution of $30,000 made by the Louisville Woolen Mills to the parent company toward the consolidated liability, and that judgment has been affirmed by the Circuit Court of Appeals for the Sixth Circuit (120 Fed. (2d) 136). A copy of the opinion of the Circuit Court of Appeals is appended to this petition as an appendix.

II.

JURISDICTION OF THIS COURT.

Section 347 of Title 28, U. S. C. A. (Section 240 of the Judicial Code), is relied upon to sustain the jurisdiction of this Court to review the judgment of the Circuit Court of Appeals for the Sixth Circuit herein sought to be reviewed. The opinion in that case was delivered on June 4, 1941. A petition for rehearing was filed in due course, and that petition finally denied by an order entered on the 9th day of October, 1941. This petition is filed within three months from that date, as provided in Section 350, Title 28, U. S. C. A. (Section 240(c) of the Judicial Code).

III.

QUESTIONS PRESENTED.

The opinion of the Circuit Court of Appeals for the Sixth Circuit holds:

(1) That the fact that the Board of Tax Appeals and the Circuit Court of Appeals had judicially and finally determined that the taxes for the year 1918 were assessable against and collectible from the parent corporation alone was not a bar to the Commissioner making a ruling on the bond that the subsidiary owed the tax individually;

(2) That notwithstanding a consolidated return by the affiliated corporations was mandatorily required by Section 240 of the Revenue Act of 1918, and notwithstanding there was an agreement between the corporations that all of the tax shown to be due by such consolidated return should be assessed against and paid by the parent corporation, nevertheless the status of the Louisville Woolen Mills, the principal on the bond, in respect of the consolidated taxes for the year 1918, was that of a taxpayer; and

(3) That the payment of $30,000 by the Louisville Woolen Mills to the parent company as a contribution toward the consolidated liability, made after the giving of the bond and after the Commissioner had ruled that a consolidated return alone was proper and that the entire tax shown to be due thereon was assessable against the parent company, and in reliance upon such ruling, did not

as of the date of payment operate to reduce the liability of the surety to the extent of such payment.

It is believed that these rulings of the Court below are erroneous, and these are the questions presented in this proceeding.

IV.

REASONS RELIED ON FOR ALLOWANCE OF THE WRIT.

(1) The Circuit Court of Appeals, in holding that the surety on a tax abatement bond was bound by the ruling of the Commissioner that the principal was liable for the taxes in respect of which the bond was executed, made after the Board of Tax Appeals and the Appellate Court had finally determined that there was no liability on the part of the principal in respect of such taxes, decided an important question of federal law which has not been, but should be, decided by this Court.

(2) The Circuit Court of Appeals, in deciding that notwithstanding the requirement of a consolidated return for the year 1918 and the existence of an agreement that the tax shown to be due on that return should be assessed entirely against the parent company, the status of the Louisville Woolen Mills in respect of the tax so assessed continued to be that of a taxpayer, decided an important Federal question in a way probably

in conflict with the decisions of other circuits and with the applicable decisions of this Court.

(3) The Circuit Court of Appeals, in deciding that petitioner, as surety on the bond, was not entitled to the benefit of the $30,000 paid by the Louisville Woolen Mills to the parent company as a contribution toward the consolidated liability, after the giving of the bond and after the Commissioner had ruled that a consolidated return alone was proper, and that the entire tax shown to be due thereon was assessable against the parent company, and in reliance upon such ruling, decided an important question of Federal law, and in a way probably in conflict with the decisions of other circuits, of the Court of Claims and of the United States Board of Tax Appeals.

V.

PRAYER FOR WRIT.

WHEREFORE, your petitioner respectfully prays that a writ of certiorari issue out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Sixth Circuit, commanding said Court to certify and send to this Court for its review and determination a full and complete transcript of the record and all proceedings of the said Court had in this case, numbered and entitled on its docket Number 8596, Royal Indemnity Company, Appellant, v. United States of America, Appellee, to the end that this cause may be reviewed and determined

by this Court, and that the decree of said Circuit Court of Appeals may be reversed, and for such further relief as to this Court may seem proper.

ROYAL INDEMNITY COMPANY,
Petitioner,

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